Southern Economic Journal

Volume I | JANUARY, 1934 | Number 2

IN THIS ISSUE—

PUBLISHED QUARTERLY BY THE SOUTHERN ECONOMIC ASSOCIATION
EDITORIAL OFFICE: 11 COMMERCE-JOURNALISM BUILDING
ATHENS :-: GEORGIA

by Mercer G. Evans

SOUTHERN WAGE DIFFERENTIALS UNDER THE NRA

One of the declared principles of the NRA program was the establishment of "fair" competition. The codes have proclaimed a large number of "fair" practices, and have prohibited a large number of "unfair" practices. In general, the tendency has been to set up standardized conditions: uniform accounting methods, uniform price-fixing policies, uniform minimum wages and maximum hours, uniform restrictions on further capital investments, uniform limitations upon the utilization of machinery, et cetera.

In the first industrial code, that for the cotton textile industry, the minimum hourly rate for the North was fixed at about the first quartile of the wage rates paid by that section of the industry in 1930 (32.5 cents) and the minimum hourly rate for the South was fixed at about the sixth decile of the wage rates paid by the Southern cotton textile employers in 1930 (30.0 cents). That is, about 25 per cent of the Northern and about 60 per cent of the Southern cotton textile workers received, in 1930, less than the minimum fixed for them.

The average of the differences between the quartiles of Northern and Southern wages, in 1930, was 14 cents an hour. The code approved a difference of 2½ cents in the minima. Whereas the South had had an advantage of about 33 per cent lower wage rates (medians compared), this was reduced to an advantage of about 8 per cent (minima compared). The South's advantage, therefore, was reduced to about 18 per cent of what it had been.[1]

In subsequent codes, and in the FERA, CWA and PWA, a similar policy has been followed. Existing wage differentials have not been entirely wiped out, but have been considerably modified, while absolute minima in both sections were generally raised. This policy has caused a clamor of protest from farm-

[1] Data compiled from Bulletin 539, U. S. Bureau of Labor Statistics. The quartile distribution of wages in the cotton textile industry in 1930 was as follows:

	1ST QUARTILE	MEDIAN	3RD QUARTILE
NORTH	32.4c	41.2c	48.8c
SOUTH	18.9c	27.7c	33.8c

ers, private employers, contractors, mayors and governors in both sections: those in the North deploring the differentials allowed, and those in the South demanding wider differentials. The Southern regional conference of the United States Chamber of Commerce demanded a 30 per cent differential for the South.

II

There are several approaches to the consideration of the economics of this wage-fixing program. Thoroughly orthodox economists, who believe that all price and wage relationships are exclusively the result of natural forces working through perfect, free competition, would say that any governmental interference is artificial and disastrous. The fact that wages in the South have been lower than elsewhere, is, for them, sufficient evidence of the lower productivity of Southern laborers. This lower productivity, furthermore, if real, is either personal or temporary. If it were due to poorer natural or capital resources, migration of labor and capital would quickly eliminate the differentials. Only the personal inefficiency of the laborers could be responsible for permanent wage differentials; and from this point of view there is nothing for the government to do, except that the more liberal of the members of this school of thought might point to wider educational efforts, or might, perhaps, be influenced by eugenicists into urging biological racial improvement.

Less orthodox economists would admit that perfect, free competition does not exist, or, that competition, while existing, is often subject to frictional delays in working out a final equilibrium. Sometimes, therefore, price relationships may be regulated, they would say, in order to establish conditions equivalent to those that would prevail if there were perfect competition.

This group recognizes two types of intervention as being justified. (a) There may be laws to compel competition, as in the Sherman and Clayton Anti-Trust Acts, and the Federal Trade Commission Act. (b) There may be laws to establish relationships equivalent to those that would prevail if there were free competition—to establish "fair" prices and "fair" wages. In this category they would justify our laws for the regulation of public utilities, and most of our minimum wage legislation. With regard to wages, it is assumed that there is some exploita-

tion of labor, especially of women and children, due to their ignorance or market ineffectiveness, and that the state is justified in demanding and getting for them all that they would be able to demand and get for themselves if they were perfectly effective in a perfectly free market.

A more modern group of economists believe in a more extensive principle of social control: they approach price and wage relationships, not only with the possibilities of imperfect competition and frictional influences in mind, but also with the idea of attempting to establish, as desired, other relationships. They are quite aware of the effects that artificial price fixation may have upon relative supplies of and demands for the factors or commodities so regulated; but they stand ready to apply the forces of social control which they have already exerted on the price ratio, to the supply and demand situations also, to provide incentives and impediments in any number of direct or indirect ways.

The recent literature of the New Deal economists seems to be based on this concept of social control. They recognize the economic limitations imposed upon them by our technological capacities and by diminishing returns from natural resources. They also recognize, however, that the effective limitations upon their programs are those of social psychology and politics. These are the forces that will limit the fulfillment of the New Deal before the administrators ever run into the difficulties of technology and natural resources. There will be constitutional difficulties over property rights, striking and soldiering by laborers, sabotaging by farmers, inventors and employers, scuttling by the technicians and capitalists, and evasions by tax-payers. These, however, are social factors, not natural economic forces.

This is not something new. Business itself had already discovered this principle. The limitations upon production and distribution have not been technological or natural: they have been the influences of social psychology that sustained the credit system, that consumed advertising, that bought automobiles for style and replacement rather than inexpensive transportation, and so on. Business itself had already undertaken social control through trying to affect the social psychology of the people. In this direction, however, business has lacked a co-ordinated program and a social purpose, and has generally failed. There

is room to hope that a more general social control, acting from a more general social motivation, may succeed.

III

The policy of the NRA with regard to national uniformity of wage minima should depend, from the viewpoint of the orthodox economist, upon, (1) whether the differences in wages in the South and North were apparent or real; (2) whether they were temporary, in the process of adjustment, or permanent; and (3) whether they were the result of artificial conditions, whether or not there really was full competition in the labor markets. Let us briefly examine these questions.

(1) As between the North and South, some students claim that living costs are lower in the South, and that this difference makes unequal money wages into equal real wages. There is no concrete evidence on the point; some studies definitely question the assertion. Other students point out that there are forms of "free income" in the South, especially in the form of employer-provided facilities in mill villages, which must be considered. This issue, too, has not been subjected to statistical investigation. It must be pointed out, however, that in many cases where employers have incurred expenses on account of the workers, the expenditures do not amount to so much free labor income. In some cases, doubtless, if the money were paid directly to the workers, they would expend it in the purchase of facilities provided by the employer; in other cases, they would not. In many cases expenditures by the employer are worth it to him (as in creating worker morale, loyalties, and so forth), but are not worth as much to the employees as the things they would buy if equal sums were given them in cash. In other cases, where the employer duplicates facilities otherwise provided for the employees, as by city governments or community chests, the duplicated facilities, costing the employer considerable sums of money, may add virtually nothing to the employees' free income.

Much of the argument concerning cost of living is based not upon differences in the costs of maintaining equivalent standards of living, but upon the costs of unequal standards of living. Some people suggest, also, that the South does not require as high a standard of living because of its customs, traditions, and environment. Sometimes this suggestion has reference to an

a priori assumption that portions of the population, either white or colored, are socially inferior and therefore undeserving of higher standards of living. All of this involves an assumption of differences in living standards and a suggestion of the desirability of maintaining a *status quo* in living standard stratification. This issue, in general, is philosophical rather than economic; most students would consider the suggestions not in harmony with democratic philosophy.

It is also suggested that unequal money wages are illusory in that they are payments for the exercise of unequal productivities by the workers. This does not have reference to marginal productivity in terms of capital equipment, but to differences in personal efficiencies. If personal productive inefficiency is biologically inherent, as many people argue with regard to, for example, the Negro, the suggestion implies that these workers are in a peculiar non-competing class. Their wages would be lower, therefore, whether they were in the South or the North. Since, however, most of the group referred to are in the South, it would suggest a lower Southern minimum. On the other hand, the Government, as an impartial, democratic body, cannot afford to endorse the principle of discriminatory wage rates based on assumption of racial inferiority unless there is fairly conclusive evidence to support its action. It is fair to say that in this case the evidence is very inconclusive.

The inefficiency may be due to climatic factors, as is suggested by Huntington. In a freely competitive society, however, the workers would, in the long-run, unless their responsiveness to the pecuniary incentive had also been dulled by climatic or other factors, migrate to the higher paid areas in the North until wages in the two sections were equal. The difference in their efficiencies would be offset by the differences in degree to which their natural resources were exploited. Southern natural resources would not be exploited to as low a margin as Northern resources, in order that the returns to capital and labor might be the same as in the North. There is nothing in this suggestion, therefore, to warrant wage differentials.

Finally, the inefficiency may be due to poorer social standards and social programs. If this is true, uniform minimum wage requirements, if too high, would tend to result in the unemployment of the sub-standard workers, and tend to create a class of "unemployables," unless other social action were taken to obviate this consequence.

(2) In general, orthodox economics has explained differen tials in terms of temporary phenomena. It is usually suggested that "natural economic forces" are at work effecting a transition, and that a permanent readjustment is on the way. It is logical to conclude, therefore, if we really have had a freely competitive economic society, that efforts of the Government to establish equal wages for competitive labor groups constitute merely an attempt to achieve quickly what would occur in the long-run from "letting nature take its course."

It has been pointed out, frequently, that the South's low wages are due to its large labor reserve, which has come into the urban industrial market through the abandonment of unprosperous agriculture. As future events promise an intensification of the South's agricultural problem, rather than otherwise, good policy would seem to indicate that steps should be taken to drain off some of the labor reserve. Orthodox economics would have it drained off through the long process of higher-wage inducements offered by the North. The NRA, on the other hand, proposes to force out the labor reserve by setting such high wage standards in the South that unemployment will result. Through employment exchanges, and other facilities, the surplus labor will then, presumably, be directed into the more profitable channels of Northern or other employment.

In so far as the wage differentials are the result of temporary transitional influences, this social action, if intelligently and energetically carried out, will shorten the period of transition. The agony of it will be more intense at the time, for both workers and owners. In the case of the workers, the Government will need to provide palliatives of relief and assistance in migration. Owners will feel the cut more sharply, though some of them are being offered, temporarily, pecuniary bribes for curtailment of their operations.

(3) Various artificial influences may be responsible for wage differentials. Environment and social traditions may offer attractions to offset higher wage inducements. If this is true, the implication is that the worker is receiving some form of natural or social "free income" that is worth the wage differential to him. Probably, workers in both the North and South are affected equally by such forces; so that the results are counter-balancing and should not influence government action.

Other sectional factors may reduce, relatively, the workers' bargaining power: a more vigorous opposition to unionism, social attitudes towards workers' "rights" and standards of living, legislation to interfere with the free exercise of collective bargaining power, or to impede free migration, and so on. It is probable that all of these factors are active in the North and South, but that they are more influential in the South. There is much less unionism in the South; there is less of a tradition of democracy concerning classes and standards of living; there are laws to embarrass emigrant agents, and governmental administrators to embarrass emigrating laborers. Southern employer groups have frequently advertised that Southern laborers were more docile. There is a definite prejudice against Negroes getting "out of their place" with regard to standards of living. Mill villages are frequently organized and administered in such a way as to impede the exercise of bargaining power and to impede migration.

The effect of a uniform minimum wage under such circumstances would be to offset the advantages accruing from such unequal artificial influences. The uniform minimum, therefore, might result in the rectification of "unfair" conditions: conditions that were "unfair" both to the Northern competitor and to the Southern laborers.

In summary, the uniform minimum wage would tend to accomplish rapidly what natural forces would accomplish, theoretically, in the long-run. To make an allowance for the possibility of differences in living costs, a small differential has been maintained in favor of the South. Otherwise, the codes will speed up the transition, and help break down artificial barriers to a natural adjustment.

IV

Two main criticisms are raised against the "high" wage minima required by the NRA program. One is that the requirement induces increased efficiency in plant management which results in more unemployment. This is probably true, and is to be desired instead of deplored. According to theory, this should eventually result in greater productivity, greater consumption power, and higher standards of living. There is no denying, however, that it causes unemployment and disorganization in the process of its accomplishment. Social agen-

cies responsible for the program, therefore, must not shirk their obligation to provide for the unemployed: first, through relief, and thereafter through rehabilitation as necessary, placement as quickly as possible, redistribution of work through shortening of hours if there is no more desirable alternative, or the provision of other economic employment through more rapid development of the market, capital equipment, or new natural resources.

It is in connection with this problem that the maximum hour provisions are provided in the codes. Partly, it is true, the administrators of the NRA believe that "it is now time for the people of the United States to treat themselves to a little civilization," as Secretary Perkins puts it. Partly, the shorter hour maxima are to provide for recreation, cultural development, and the like. Primarily, however, they were to provide for "job-sharing," a redistribution of employment among a larger number of employees.

This, of course, is not the only alternative. If society wants more goods, rather than more leisure, we are not over-capitalized, and all labor made idle by more efficient plant management can be put to work increasing the quantity of goods to be consumed. The determination of this problem depends upon such factors as the distribution of income, the debt situation and price ratios, and so forth. Its solution is not now subject to very effective social control, but there is no reason why it may not be subjected to complete social control if the Government and the people decide that they want to use that method in solving such problems.

The other criticism is that the high minima cause employers to displace the sub-standard workers with a smaller number of more efficient workers, thus, again, increasing the number of unemployed, and creating, also, a class of relative unemployables. This criticism is raised in the South especially with regard to Negroes. In so far as it is true—and it may be that much of the displacement of Negroes is due more to race prejudice than to their lower efficiency—it can be said that, as long as someone has to be unemployed, it is better that it should be the sub-standard workers. In the first place, the decline in the standard of living that results from going off the job and on to the relief roll is not so great. In the second place, the loss in efficiency resulting from unemployment is less. In the third place, it definitely poses society's problem—that a portion

of the population is unable, because of personal inefficiency, to earn a subsistence minimum wage, and, since these laborers are now unemployed and totally dependent, society must do something about it. This will call, among other things, for social action to improve health conditions, to raise sanitary standards, to provide more formal and vocational education, to effect personal and social rehabilitation, including recreation and housing.

The major complaint against the NRA labor program, however, is directed at the "high" wage minima as such. It is claimed that industry cannot bear the charge, and that Southern prosperity will be destroyed. It would, of course, be possible to fix higher real wage minima than American industry can or will produce under present incentives; but there is no reason for supposing that the minima of any of the codes approach anything of this nature. The answer can be discovered, however, only through experimentation.

It is possible, of course, that a movement of labor from the South to the North might lower the marginal productivity of Northern labor more than enough to offset the gain in Southern marginal production. In this case, "other things being equal," labor as a whole would suffer a net loss; Southern labor, nevertheless, would gain. It is possible, also, that current minima will exceed the wages that can be paid by some industries in the South, unless they curtail their margin of production, or improve their productive efficiency. Under this pressure many managements will undoubtedly find ways to increase their efficiency. We may see an improvement in the efficiency of household management in the South, as a result of the high wages that will have to be paid domestic servants on account of the competition offered by the high wage industrial employments, and quasi-guaranteed by the FERA and CWA. On the other hand, many marginal business firms, perhaps, will be forced out of business, including many farms. This will not occur all at once, but will await for its final completion the total depreciation or obsolescence of the marginal capital investments.[2]

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[2] The reader is referred to the paper of Ewan Clague, "Unemployment as a Permanent Social Problem," read at the December, 1933, meeting of the American Economic Association, for an excellent discussion of the problems treated above. Mr. Clague suggests that the economic and social developments of the depression forecast a heavy burden of unemployment, if not of unemployables, for some years to come.

V

The validity of the uniform minimum wage must be considered in the light of the whole program of social control. Before casting judgment upon it, consideration should be given, for example, to such possible exercises of social control as the following:

(1) Decreasing the total labor supply—by means of the prohibition of child labor, the restriction of woman labor under certain conditions, the superannuation of older people on pensions, the sending of the half-sick to hospitals and of the poorly trained to schools, the encouragement of lengthy vacations for recreation and industrial recuperation, and the shortening of the hours of work for all laborers.

(2) Redistributing the labor force—by means of employment exchanges, aids to transportation, vocational rehabilitation, and pecuniary inducements to the migration of labor from employments of less marginal productivity to those of greater marginal productivity.

(3) Increasing the personal efficiency of labor—by means of health and educational programs, reconstruction of housing and social environment, new recreational activities, and by heightening the standards of living through higher wage or relief incomes.

(4) Improving the efficiency of management and plant—as a result of the requirement of higher wage payments, through regulation of competition and organization of firms into associations for exchange of information, allocation of production, etc., and through elimination of wasteful production and idle equipment.

(5) Controlling the supply of capital—through taxing out of corporate surpluses, requirement of permits of necessity and convenience before investment, regulation of security selling, and, if necessary, social saving, effected by taxation.

(6) The development of whatever incentives may be necessary, cognizant of the future, to replace the supposed effectiveness of the so-called profit motive; establishment of national planning boards, development of a high-toned civil service, broadcasting of a new education concerning our politico-economic organization, and so on.

To the extent that real wages are raised, the increase will have to come, of course, in the final analysis, from one or both of these sources:

(a) Greater productivity: the result of greater personal

efficiency on the part of labor, a more efficient distribution of labor, more efficient management, the investment of more, or of more effective capital equipment, the more effective use of capital already invested, or better development of natural resources.

(b) Redistribution of income: through elimination of exploitation, or through measures of social control which cause higher wages to be paid without permitting a contraction of capital or natural resources. Aside from such methods as taxation, this can be done, of course, only by violating the concepts of capitalistic economy. Neither of these sources of higher wages has as yet been more than barely tapped by the New Deal.

In essence, we are faced with the choice of two methods of social control: one is to recognize and crystallize *status quo* and, while trying to maintain free competition, depend very largely upon natural forces to effect such changes as were already in store for us; the other is to assume relatively complete social control, and to mold economic society into the desired pattern. The former is the ideal of the Sherman and Clayton Acts; the latter is the principle of the "New Deal." It would obviously be impossible, in an orthodox economic system, to establish a wage minimum higher than that justified by marginal productivity without expecting more unemployment or other difficulties. The Government, however, seems to have no delusions about breaking orthodox economic laws in an orthodox economic society. It is creating an economic society based on social control, and not dependent upon the motivations of the past century. The Government appears to stand ready to supply whatever additional forces of social control are necessary, at whatever points, in order to make effective those forces that it has already applied. If the high wage minima cause unemployment of the sub-standard workers, it may undertake the work of raising the efficiency of these workers to the approved norm. If the minima cause sectional unemployment, the Government may undertake the transportation of the surplus labor to other sections. If the minima encroach upon the returns to capital sufficiently to contract seriously the supply of capital, the Government may undertake to meet that exigency through various methods of social saving. This does not mean that the Government has committed itself to socialism; but the Government does seem to have committed itself to take whatever social action is necessary to achieve its declared end of providing all portions of the population with a certain minimum standard of living.

by C. K. Brown

THE FINANCIAL CONDITION OF RAILROADS IN THE SOUTH IN 1933

The depression appears to have dealt more severely with the railroads of the South than with those of any other section. In 1931 only four out of 21 Class I railroads in the Southern region earned all their fixed charges. As a group these roads failed by $22,000,000 to earn their fixed charges of $86,-000,000. In 1932 only one of these roads (the Clinchfield) earned its fixed charges, and the roads as a group failed by over $48,000,000 to earn fixed charges of $87,000,000. The Southern roads as a whole thus earned 74 per cent of their fixed charges in 1931 and 44 per cent in 1932.[1] The roads of no other section show so poor a record for these years. In both the eastern and the western sections the roads as a whole more than earned their fixed charges in 1931. In 1932, 19 out of 52 Class I roads in the East earned all fixed charges, and the group as a whole earned over 98 per cent of fixed charges.[2] In the West 10 out of 46 Class I roads earned all fixed charges, and the group as a whole earned 63 per cent of fixed charges.[3]

One accompaniment of this extremely poor showing in the South was that seven of the 21 Class I roads of the South found themselves in receivership on July 1, 1933.[4] These seven roads operate more than 10,000 miles of line, or slightly more than one-fourth of the entire mileage of the section. Moreover, these seven roads account for nearly one-half of all mileage in the country in receivership. Included in the Southern receiverships however, are several chronically weak roads, such as the Seaboard and the Norfolk Southern. These two roads account for more than half of the Southern mileage in receivership.

The railroads of the South have relied upon loans from the Reconstruction Finance Corporation to a smaller extent than have the roads of other sections. This has been due, no doubt, to their relative inability to offer acceptable security for such

1 Statistical Exhibits filed on behalf of the carriers by the Bureau of Labor Statistics, in I. C. C. Docket 26000, May, 1933, Sheet 13.
2 *Ibid.*, Sheet 12.
3 *Ibid.*, Sheet 14.
4 "Railroads in Receivership July 1. 1933," Bureau of Labor Statistics.

loans. At the end of August, 1933, eight Class I roads in the South owed the Reconstruction Finance Corporation a total of $26,000,000, which constituted only about one-twelfth of all loans made by the Corporation to railroads.[5] Of this sum of $26,000,000 the Southern Railway Company owed nearly $15,000,000 and the Illinois Central more than $6,000,000. It thus seems that the South, which stood in greatest need of such loans, has been benefited to the smallest extent and has had to resort to receiverships more widely than any other section. The explanation is no doubt to be found in the fact that the depression struck the Southern roads long before those in other sections began to feel its force. The weak Southern roads were either already in receivership or else on the verge of it when the Reconstruction Finance Corporation began to function early in 1932. Of the seven Class I roads of the South now in receivership, none earned its fixed charges in 1932 or 1931, only one in 1930, and only four in 1929.[6]

From 1929 to 1932 operating revenues declined by approximately the same percentage in all sections of the country.[7] In the East (including the Pocahontas region) the decline was 49 per cent, in the South 51 per cent, in the West 52 per cent. But while 1929 was the peak year for revenue in the West, 1926 was the peak year in both the East and the South. In the East total operating revenues were 2.25 per cent lower in 1929 than in 1926. In the South they were 12.4 per cent lower in 1929 than in 1926. If the decline to 1932 from the peak year in each section be taken, it appears to have been 50 per cent in the East, 52 per cent in the West, and 57 per cent in the South.

If freight and passenger revenue be separated, it appears that freight revenue declined 9.13 per cent in the South between 1926 and 1929, against a decline of 1.27 per cent in the East and an increase in the West. Between 1929 and 1932 freight revenue declined 48.8 per cent in the South, 48.3 per cent in the East and 50.4 per cent in the West. Passenger revenue in the South fell 32 per cent between 1926 and 1929, against declines of 11.5 per cent in the East and 16.8 per cent in the West. Between 1929 and 1932 they fell an additional

[5] Report of Reconstruction Finance Corporation, released to morning papers of Sept. 3, 1933.
[6] Statistical Exhibit, *op. cit.*, Sheet 13.
[7] The percentages in this and the following paragraph have been calculated from the figures given in "Statistical Exhibits," *op. cit*, Sheets 4, 5, and 6.

64.3 per cent in the South, compared with declines of 52.2 per cent in the East and 62 per cent in the West.

Two facts thus stand out from these figures: (1) Freight revenue declined very decidedly in the South between 1926 and 1929 while it remained approximately stable in the rest of the country. (2) Passenger revenue declined much more sharply in the South than in any other section in the three years before 1929 and has continued to decline more rapidly since 1929. A satisfactory explanation of these divergencies would throw much light upon the entire topic of Southern economy. It is customary to say that the collapse of the Florida boom in the middle twenties accounts for the declines in both freight and passenger revenue prior to 1929.[8] That this circumstance played an important part is not to be denied, but negative explanations should be used only in support of positive ones where the latter can be advanced. With regard to passenger revenue two other factors may be mentioned. One is climatic. The milder climate of the South no doubt encourages the use of the automobile for travel in the winter season, while in less hospitable regions the railroad would be a preferred mode of travel. The other factor is that of density of population. The hypothesis may be advanced that there is a certain medium density of population which is most conducive to the use of the automobile in lieu of the railroad. In areas of denser population the private automobile becomes a nuisance to its operator and can be employed with neither speed, economy, nor comfort. In sections where population is very sparse, distances great, and towns far separated, the railroad will be preferred by many persons. The automobile is most serviceable where traffic is not excessively heavy, parking not too laborious, nor communities too far separated. The South probably meets these conditions on the whole better than any other section of the country.

The decline of freight traffic in the South between 1926 and 1929 should probably be taken as indicative of the divergence that exists in the pace of economic activity between areas which are economically discrete although included in the same national economy and comprising portions of the same free trade territory. The South is heavily dependent upon two non-food agricultural annuals, cotton and tobacco, of which she normally exports about half. Her prosperity is peculiarly

[8] Cf. e. g., Moulton, et al, *The American Transportation Problem*, p. 35.

dependent upon both the weather and the state of foreign markets. Her manufacturing industries are overwhelmingly devoted to the production of commodities for final consumption, which notoriously do not show the same cyclical movements as the heavier industries devoted to making more durable goods. Without going further into the specific manner in which these peculiar conditions may be held to account for the downturn in traffic after 1926, it may be insisted that important forces can here be found to add to the influence of such fortuitous occurrences as the collapse of the Florida boom.

Some support for this conclusion is found in recent revenue statistics.[9] Relative to 1931 freight revenue for 1932 declined very slightly more in the South than in the country as a whole. Beginning with the first month of 1933, however, freight revenue in the South has made a better showing than in the country as a whole. For the first three months of 1933, which are usually considered to have been the low point of the depression, freight revenue in the entire country was 18 per cent below that for the corresponding period of 1932, while in the South it was only 11.8 per cent below. For the first eight months of 1933 the figures show an increase of 6.1 per cent in the South against an increase of less than 1 per cent in the country as a whole. Passenger traffic, although continuing to decline in 1933, has declined less in the South than in the rest of the country. The declines in passenger revenue for the first eight months of 1933 were 17.7 per cent for the South and 19.7 per cent for the United States.

The decline in tonnage handled has, of course, not been uniform in all the commodity groups, with the result that the composition of the traffic handled has changed somewhat within the past several years. It is quite remarkable, however, that it has changed as little as it has. Between 1929 and 1932 revenue from forest products handled by the Southern railroads declined from 13.26 per cent of total freight revenue to 7.61 per cent. Manufacturers and miscellaneous declined only from 29.09 per cent to 27.69 per cent. All other categories increased their proportion of the total, with the largest increases in agricultural and animal products. It is

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[9] *Railway Revenues and Expenses*, Mo. Rept. Ser. Bureau of Labor Statistics. August, 1933.

interesting to note that revenue from L. C. L. freight was 13.5 per cent of the total in 1929 and 14.02 per cent in 1932.[10]

To express essentially the same facts in another fashion, we may say that tonnage of forest products declined between 1929 and 1932 by 71 per cent, tonnage of animal products by 31 per cent and the tonnage in remaining groups by figures lying between 38 and 54 per cent. These figures seem to indicate a balance in the economy of the South that is not to be found in any other major section of the country. The dispersion of the percentage declines in the six commodity groups was much less in the South than in any other section. The average deviation from the mean was 9.9 for the South, 16.1 for the East (exclusive of the Pocahontas region), and 14.4 for the West. The decline thus appears to have been much more evenly spread over all the commodity groups in the South.

To meet the declines in revenue the Southern roads have reduced operating expenses drastically since 1929, although not quite so drastically as in the East or West. The difference is no doubt due to the fact that the Southern roads had already reduced operating expenses considerably between 1926 and 1929. In no section have the reductions in expenses been commensurate with the decline in revenue, with the result that, down to 1933, operating ratios rose in every part of the country. Since revenues have declined most in the South operating ratios have risen most here, namely from 73.91 in 1926 to 82.69 in 1932.[11] This high operating ratio explains the relatively greater failure of the Southern carriers to meet their fixed charges.

It is clear that the railroads of the country could not have reduced operating expenses as they have done without postponing much of the heavier repair work to roadway and equipment. But there is no evidence that the Southern roads have maintained their properties less adequately than the roads of the East and the West. In many cases these postponed expenditures for maintenance must be expected to absorb a large part of the total revenues when once more an increase in traffic shall have removed the more pressing problem of meeting fixed charges. This is to say that in the absence of an abnormally rapid increase in revenue the outlook

10 Statistical Exhibits, *op. cit.*, Sheets 24-27.
11 *Ibid.*, Sheet 5.

for the holders of railroad equities within the reasonably near future is not particularly bright.

The greater difficulties of the Southern railroads are not due to excessively high fixed charges as compared with other sections. There are no significant differences among the sections in the proportion of capitalization represented by bonds. The ratio of fixed charges to capitalization is approximately the same in all sections, as is their ratio to average revenues over a period of years. Of course, it may be urged that all our railroads have too high a proportion of their capitalization represented by bonds, but this at bottom is a matter of the distribution of corporate income, which is of concern to the holder of junior claims on income, but whose importance to the shipping public or to general economic development is likely to be overemphasized. A railroad does not cease to serve the community just because the bondholders receive all the income and the stockholders nothing. Indeed it continues to operate even though the bondholders do not receive all that their bonds promise them. Only if the rate-making authority considers the payment of interest on bonds more imperative than the payment of dividends on stocks does the ratio of bonds to stock make any difference to the shipping public.

It is customary to say that the level of freight rates in the South is considerably higher than in the East and that Southern economic development has been retarded by this circumstance. But this is a crude generalization, which, if it could be demonstrated to be true, might not be so significant a factor in Southern economy as is commonly supposed. The average revenue per ton-mile of freight in the South is very close to the corresponding figure for the entire country.[12] But this means nothing, since the composition of the traffic varies considerably from one section of the country to another. It is not so easy to demonstrate that freight charges are higher in the South relative to the value of the commodities handled. It is, of course, possible to compare class 4 rates for 200 miles in the South with class 4 rates for 200 miles in the East, but the same commodities do not in all instances move as class 4 in the two territories. And even if they did, the result of the comparison would be misleading, since the significance of the

[12] In 1932 the figures were 1.089 cents for the South against 1.045 for the U. S. *Ibid.*, Sheet 29.

commodities in the entire economy of the region would be quite different in the two instances.

After all, transportation cost is only one item of cost in doing business, and it is the totality of production costs which determines the profitableness of industry and the pace of its development. This is ultimately a matter of topography, climate, natural resources, and the efficiency of labor, from the operation of which factors the transportation agencies themselves are not exempt. Since railroad rates are subject to determination by public authority, we fall into the habit of thinking that here is an item of cost which can be regulated by governmental fiat, and which consequently should be regulated downward to offset any other unfavorable items of cost. We are inclined to blame high transportation rates for many competitive disadvantages which are properly chargeable to other items of unfavorable cost. The railroads not only should not be operated for the purpose of equalizing costs among private businesses otherwise variously situated, but except within very narrow limits they cannot be so operated. On the other hand, the railroads are not entitled to any particular rate structure solely because it will maintain or come nearest to maintaining the existing capital structure of the railroads. We are in especially grave danger of adopting this attitude in a period of depression when one of the government's most evident objectives is the maintenance of existing capital structures. Rate-making policy should not pay too much attention to past investment in the railroad business. It is not a legitimate function of government to attempt the maintenance of past investments in railroads, since the attempt involves a levy upon the shipping industries and thereby impairs the past investments in those industries. A proper rate-making policy looks chiefly to the future.

In so far as the sale of transportation services is subject to equitable competition by motor vehicles, as has increasingly been the case, the railroads are, broadly speaking, entitled to what they can get and no more. Public regulation should permit the railroads to lower charges to meet such competition if they can still cover out-of-pocket, otherwise the railroads must abandon the traffic to the more efficient agency. Where the privilege of monopoly is enjoyed, rates must be maintained at such a level as will assure the future provision of transportation facilities of such type and number as may

reasonably be deemed necessary. There is no rule of thumb whereby such rates can be arrived at. But however arrived at, the rate structure should probably not be subjected to violent disturbances. This means that in times of depression we should not expect considerable readjustment of freight rates to meet changes in commodity prices. The ratio of transportation costs to total costs should be allowed to rise. This will generally be a lesser evil than the disturbance of the multiple relationships, geographical and commercial, which are involved in a freight rate structure, and which it is impossible not to disturb when wholesale revision of rates is undertaken. Inflexibility in the price system is responsible for many of our difficulties, but in this case it seems to be justifiable as the lesser of two evils. As with taxes, there is a measure of truth in the statement that any old rate structure is a good one.

There is no immediate prospect of reduction of rates in the South, although an Interstate Commerce Commission examiner has suggested certain adjustments in the border regions of North Carolina and Kentucky.[13] The railroads have calculated that a general reduction of the tariffs would by no means sufficiently stimulate traffic to make up for the loss of revenue. The Bureau of Railway Economics estimates that a 60 per cent increase in traffic would be necessary to offset the loss of revenue from a 25 per cent reduction in rates.[14] When the railroads refuse to believe in the efficacy of reduced rates, they are simply saying that they consider the level of freight rates only a minor factor in the determination of the volume of traffic moving. This conclusion is very probably correct. Both the railroads and the shippers must ride out the present depression with the present system of rates. As for the shippers, the level of freight rates is far from constituting their greatest difficulty, so far indeed that a reduction of freight rates could not be expected to produce a significant degree of recovery. As for the railroads, a moderate increase in traffic would rapidly restore them to solvency as a group, especially in view of the fact that many of the economies inaugurated during the depression will likely prove to be permanent. There is no reason for thinking that a considerable improvement in traffic will not accompany even a mod-

[13] See *Traffic World*, Sept. 23, 1933, p. 499, and Sept. 30, 1933, p. 545.
[14] Statistical Exhibits, *op. cit.*

est prosperity, although the traffic levels of the 1920's may not again be attained for many years. If traffic does not increase in the near future more of the roads will be forced into bankruptcy or else will have to rely heavily upon loans from some government source, which may turn out to be a method of selling the railroads to the government. There has, it is true, been considerable improvement in the net railway operating income of the roads of the South in 1933. It was over $38,000,000 for the first eight months of the year as compared with $7,000,000 in the corresponding period of 1932.[15] But this has been due chiefly to a further reduction of operating expenses below the already low levels of 1932 and only moderately to an increase in traffic. Indeed the increase in traffic apparent for the first two-thirds of the year as compared with 1932 may be wiped out for the full year unless the recession in business activity since August is soon checked.

Fortunately for the railroads they have not had their wage costs increased as have those businesses which are operating under the National Recovery Administration codes, but if the rise in prices now being engineered by the federal government should take a decidedly speculative turn, and especially if it should get out of hand, it is conceivable that railroad costs, including wages, might rise more rapidly than revenues under the relatively inflexible rate schedules. Certainly this was the experience of the railroads with the rapidly rising prices of the first post-war boom.

In discussions of current topics such as those with which this paper deals we are prone to take a far too narrow view of the significance of outward evidences either of distress or of prosperity. We dwell upon the importance of surface ripples and ignore the deep underlying swells. Most of us call our present condition depression and confidently look forward to a return to the business plateaus of the twenties. But the present condition might be described as the collapse of an industrial and nationalistic economy, which after having driven toward economic futility for a generation or more has concluded that its salvation lies in a stricter economic nationalism. In the present disorganized state of both domestic and world economy it is almost impossible to assess the immediate

[15] *Railway Revenues and Expenses*, Mo. Rept. Ser. Bureau of Labor Statistics, Aug., 1933.

prospects for the railroads of the South. These immediate prospects may not, however, be of such transcendent importance. Perhaps this much we may say with some assurance: the railroads of the South are a part of the entire Southern economy and are likely to prosper or to fail to prosper with it. The South with her cotton and tobacco is more committed to the export business than any other section of the country. If the present nationalistic economics continues in vogue, the prospect is not very encouraging for the South, nor for her railroads.

by Alfred W. Garner

A NOTE ON THE MISSISSIPPI SALES TAX

On January 1, 1932, the state of Mississippi was burdened with an accumulated deficit of approximately $8,000,000. The total debt of the state was over $50,000,000. The returns from the state income tax in 1932 were less than one-fourth of what they were in 1928. The income from real property had slumped to the point where the owners in many cases were not able to pay their taxes at the current rate. The credit of the state was about gone; its bonds could not be sold. During the session of the legislature in 1932 an Emergency Revenue Act, commonly called the Sales Tax, was passed. This law provided for the levy of a 2 per cent retail sales tax to go into effect May 1, 1932.

While the economists are disposed to say that most new taxes are bad ones, and to condemn sales taxes particularly, it is interesting to note that for Mississippi at least only good results are in evidence after 18 months of operation. The tax has produced, even during the depression, revenue even beyond the estimate of its advocates. For the first eight months it was in operation in 1932, the yield exceeded the estimate for the entire year by $235,507.41. The revenue from it for the present year will, no doubt, be considerably more than it was in 1932. For instance it brought in for the month just closed, November, $284,233.38, while the monthly average for the year was set at $166,666. And this increase will be much greater during the month of December.

The tax since going into effect has increased the revenue of the state about 25 per cent. It has enabled the state to balance its budget, to meet its obligations as they have matured; and has been the means of restoring its credit. It looks as though it has toned up the entire revenue system of the state; people seem to be paying other taxes more readily, even before business recovery. For instance, there was a balance in the state treasury November 1 of $1,991,740.90, which was very unusual for the state of Mississippi.

The salvaging of the state government as such has been achieved and it seems quite unlikely that anyone has been hurt by the burden of this new tax, for in 1932 the per capita monthly

payment was only 9.7 cents. The load is too small to be noticed. There certainly has been no noticeable increase in the cost of living traceable to the tax; nor any appreciable loss of business to foreign mail order houses. Neither have there been any harmful reinvestments and shiftings of capital or any dangerous integrations of business. These are some of the most tangible and pleasing results to the Mississippians that have come from this new tax.

This tax is condemned by most present day economists as being a bad tax, possessing, among other evils, a regressive feature which exacts more of the poor man's small income for the necessities of life than of the large income of the well-to-do. Yet it seems that it is only by the help of this outlawed member of the taxing family that Mississippi has been able to put its tax system on a basis of equity and justice. To say that 85 per cent of the people in the state that pay no property tax, regardless of race or the amount of intangible property possessed, bear their share of the tax burden indirectly is certainly a large assumption. The state of Mississippi acted upon some such theory until it found itself on the verge of bankruptcy.

The general sales tax is not only forcing every buyer to contribute something to the support of the government, but it may even be contended that in its operations it tends to equalize the general burden among individuals possessing different abilities to pay and between the rural and city dwellers as well as between the different sections of the state.

For instance, if more of the intangible property which is concealed from the taxing authorities, as has been proved by the states having a general property tax, is found in the cities than in the rural communities it will be seen, other things being equal, that the rural dweller pays more than a proportionate share of the old property tax. But in the case of the general sales tax the heavier burden falls upon the city dweller. Thus the tendency is to equalize the burden.

For instance, in one of the most rural counties in the state the average monthly per capita sales tax burden for 1932 was only .7 cents. On the other hand, in the most urban county in the state the monthly per capita tax burden was 25.5 cents, or more than 36 times as great as it was in the rural county.[1]

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[1] These counties are Hinds (25.5) and Benton (.7), and the averages come from the Report of the State Tax Commission for 1932.

These two counties represent the two extremes, it is true, and there were a number of factors in this case that helped to cause this difference. Yet a very striking difference is shown by a comparison between any of the other counties containing cities with those having none.

The small per capita payment of the rural dweller as compared with his city neighbor does not necessarily mean that the standards of living of the former are lower than those of the latter. It may mean that the farmer grows more food crops for home consumption to escape the heavy part of the sales tax burden. In this way his standard of living would be pushed up since he would not only have more things to eat but would be left with money formerly spent for food with which to purchase clothes, other necessities and luxuries. That such is highly possible may be seen from the state tax commission report, showing that one of the large items for which the people spend their money is food. Also the federal census report indicates that the farmers in the county in which the sales tax burden was only .7 cents per capita per month, as cited above, used farm products grown at home in 1929 valued at $446,063.

Furthermore, there is a difference in the sales tax burden borne by the people living in different sections of the country and employing different types of farming.

In the Mississippi-Yazoo delta the plantations are large, representing heavy investments, and as a general rule are tilled by negro tenants. On the other hand in the hill regions the farms are usually small in size, representing small investments and, in the main, tilled by their owners. The sales tax burden runs higher in the delta counties than in those in the hills. In 13 delta counties, containing their trade centers with a population of 491,050, the monthly per capita average burden in 1932 was 9.38 cents. While in 21 hill counties, containing their trade centers, with a population of 493,758, or approximately equal to that of the 13 delta counties, the sales tax burden per capita monthly, averaged only 6.58 cents.[2]

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[2] The delta counties are: Warren, Issaquena, Yazoo, Humphries, Washington, Leflore, Sunflower, Bolivar, Tallahatchie, Quitman, Coahoma, Tunica, and Sharkey.

The "hill" counties are: Alcorn, Tishomingo, Prentiss, Union, Pontotoc, Lee, Itawamba, Calhoun, Chickasaw, Monroe, Webster, Clay, Choctaw, Oktibbeha, Lowndes, Winston, Noxubee, Neshoba, Kemper, Newton, and Lauderdale, and *Ibid.*

But the property tax is also notoriously regressive, which means that, other things being equal, the hill farmer pays a higher proportionate tax on his land and the appurtenances thereto than his delta neighbor does. Again the sales tax tends to offset this difference by placing a smaller burden where the property tax falls the heavier, and vice versa. Furthermore, of the sales tax burden that falls on the delta section a considerable part is borne by the negroes who pay very little or no other taxes.

As may readily be seen, this same tendency toward an equalization of the burden of taxation will take place throughout the state even among persons living in the same communities owning real properties of greater and of smaller values.

Thus it may be seen that in Mississippi the general property tax and the general sales tax, the two taxes that are most severely condemned by the classical economists, are working well together in the tax system of the state. The state has had an income tax since 1924.

The Southern Economic Journal is published quarterly under the auspices of the Southern Economic Association. Editorial communications should be addressed to: 11 Commerce-Journalism Building, The University of Georgia, Athens, Georgia.

The subscription rates are: single copies 75 cents; institutional subscriptions, $3.00 annually; individual Association memberships (including the Journal) $2.00 annually.